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In the Supreme Court of the United States

OCTOBER TERM, 1997

NYNEX CORPORATION, ET AL., PETITIONERS

v.

DISCON, INCORPORATED, RESPONDENT

On Writ of Certiorari to the United States Court of Appeals for the Second Circuit

MOTION FOR LEAVE TO FILE BRIEF AND BRIEF FOR THE AMERICAN AUTOMOBILE MANUFACTURERS ASSOCIATION AS AMICUS CURIAE SUPPORTING PETITIONERS

PHILLIP D. BRADY
MARK SLYWYNSKY
American Automobile Manufacturers Association
1401 H Street, N.W.
Suite 900
Washington, D.C. 20005

STEPHEN M. SHAPIRO
ROY T. ENGLERT, JR.
Counsel of Record
DONALD M. FALK
MICHAEL E. LACKEY, JR.
Mayer, Brown & Platt
2000 Pennsylvania Ave., N.W.
Washington, D.C. 20006
(202) 463-2000

Counsel for Amicus Curiae

HPP

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MOTION OF THE AMERICAN AUTOMOBILE MANUFACTURERS ASSOCIATION FOR LEAVE TO FILE BRIEF AS AMICUS CURIAE SUPPORTING PETITIONERS

Pursuant to Sup. Ct. R. 37.3, the American Automobile Manufacturers Association ("AAMA") respectfully moves for leave to file the accompanying brief as *amicus curiae* in support of petitioner.[1] Petitioners have consented to the filing of the brief; counsel for respondent has consented orally to the filing of this brief, but AAMA had not received written consent by the time the brief was sent to be printed. See Sup. Ct. R. 37.3(a).

The American Automobile Manufacturers Association ("AAMA") is a non-profit national trade organization. Its member companies — General Motors Corporation, Ford Motor Company, and Chrysler Corporation — are the largest automobile manufacturers in the United States. The AAMA has often represented its members before this Court.

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[1] This brief was funded entirely by the AAMA and was authored entirely by its counsel.

The first question presented in this case provides two important and related opportunities to clarify the antitrust laws. First, this case calls for an evaluation of the vitality and proper scope of the *per se* prohibition of "group boycotts." Second, the Court can and should continue to clarify the status of vertical nonprice restraints.

The AAMA wishes to present its views on these issues because they are of exceptional significance to its members. Vertical restraints — agreements between firms at different levels of distribution — are important competitive tools for all manufacturers that face intense interbrand competition. Manufacturers use a variety of vertical agreements to obtain inputs with the greatest efficiency and at the lowest price. Vertical agreements are particularly important to manufacturers that, like AAMA members, distribute their products to the public through a network of independent local dealers.

The AAMA addresses these issues from the perspective of the domestic automobile industry to assist the Court in its assessment of the real-world consequences of the resolution of this case. The AAMA supports its views with examples from its members' experience competing in an industry marked by intense interbrand competition at the producer level. That experience has shown the importance of flexibility in commercial arrangements with parties at different levels of distribution. AAMA members can produce automobiles more efficiently if they are able to deal with sole-source or limited numbers of suppliers who have strong incentives to satisfy the standards of the industry. Similarly, manufacturers have promoted the efficient distribution of vehicles to consumers by imposing limits both on the number of authorized distributors and on their conduct. The possibility is remote that these vertical restraints could have any adverse effect on interbrand competition.

By contrast, hostility to such arrangements — whether it takes the form of the *per se* condemnation suggested by the Second Circuit in this case, or the condemnation after cursory

analysis that the government suggested in its *amicus* brief at the certiorari stage — threatens the efficiencies resulting from exclusive or limited supply and distribution agreements. Such arrangements should continue to be subject to full rule-of-reason review, with the accompanying presumption of legality.

For the foregoing reasons, the motion of the AAMA to file the accompanying brief as *amicus curiae* in support of petitioners should be granted.

Respectfully submitted.

PHILLIP D. BRADY
MARK SLYWYNSKY
American Automobile Manufacturers Association
1401 H Street, N.W.
Suite 900
Washington, D.C. 20005

STEPHEN M. SHAPIRO
ROY T. ENGLERT, JR.
Counsel of Record
DONALD M. FALK
MICHAEL E. LACKEY, JR.
Mayer, Brown & Platt
2000 Pennsylvania Ave., N.W.
Washington, D.C. 20006
(202) 463-2000

Counsel for Amicus Curiae

JUNE 1998

QUESTION PRESENTED

This brief addresses the first question presented:

Whether, by dealing with one supplier, a purchaser engages in a "group boycott" of the supplier's disappointed competitors, and thus may be subjected to *per se* liability under Section 1 of the Sherman Act.

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BRIEF FOR THE AMERICAN AUTOMOBILE MANUFACTURERS ASSOCIATION AS AMICUS CURIAE SUPPORTING PETITIONERS

INTEREST OF THE AMICUS CURIAE

The American Automobile Manufacturers Association ("AAMA") is a non-profit national trade organization. Its member companies — General Motors Corporation, Ford Motor Company, and Chrysler Corporation — are the largest automobile manufacturers in the United States. The interest of the AAMA is described in detail in the motion for leave to file this brief, *supra*.[1]

INTRODUCTION AND SUMMARY OF ARGUMENT

This Court has repeatedly narrowed the scope of business conduct that may be condemned *per se* under the antitrust laws — *i.e.*, condemned without proof of anticompetitive effects in a relevant product and geographic market, and without consideration of possible justifications. In particular, the Court has removed the *per se* stigma from all vertical *non*-price agreements that affect only a single manufacturer's

[1] This brief was funded entirely by the AAMA and was authored entirely by its counsel.

products, and even from vertical *price* agreements that set a maximum resale price for a single brand. Furthermore, the Court no longer condemns *per se* certain horizontal agreements that produce a common price. If the competitors who participate in the agreement are engaged in a legitimate, procompetitive joint venture, the Court recognizes that ancillary agreements on price may be lawful.

In the decision under review, the Second Circuit placed itself at cross-purposes with these trends toward greater flexibility for businesses engaged in efficiency-enhancing activities. The court transformed a garden-variety contractual relationship between two firms into a potential *per se* antitrust violation by mislabeling the contract a "group boycott" of a disappointed competitor.

An agreement by one firm to buy from another (and thus not from a third) may be an exclusive-dealing arrangement, but by no stretch of the imagination is it a "group boycott." The Second Circuit's error was in some ways understandable, however. This Court has not expressly disavowed some unfortunate language in two early boycott decisions: *Klor's, Inc.* v. *Broadway-Hale Stores, Inc.*, 359 U.S. 207 (1959), and *United States* v. *General Motors Corp.*, 384 U.S. 127 (1966). *Klor's* and *General Motors* in large part have been superseded doctrinally by the more sophisticated analysis in later cases, but the two cases continue to add confusion to a very muddled area of law. It is important that the Court explicitly describe the current scope of the *per se* rule against group boycotts.

In *FTC* v. *Superior Court Trial Lawyers Ass'n*, 493 U.S. 411, 436 n.19 (1990), the Court suggested that *per se* treatment is now reserved for boycotts in the service of price-fixing agreements. If correct, that understanding should be made explicit in this case. In any event, the Court should make clear, *first*, that the *per se* rule against group boycotts covers only concerted refusals to deal with a supplier or customer by competitors of the victim of the boycott, and, *second*, that a concerted refusal to deal within a vertical

context (as among distributors of a single brand in a multi-brand market) is subject to rule-of-reason analysis just like other vertical nonprice restraints.

Full rule-of-reason analysis — not a "quick look" — should apply. The Court should reject the suggestion of the United States that the choice of one supplier rather than another might be condemned under a truncated rule of reason analysis when neither interbrand market power nor anticompetitive effects in a relevant market have been alleged or proved.

Finally, this Court should reaffirm that facially deficient antitrust claims can and should be dismissed for failure to state a claim. It is not appropriate for courts to develop novel, unpleaded and unbriefed legal theories in order to prolong antitrust lawsuits brought by disappointed competitors.

ARGUMENT

"[M]ost antitrust claims are analyzed under a 'rule of reason,' according to which the finder of fact must decide whether the questioned practice imposes an unreasonable restraint on competition" under the circumstances of a particular case. *State Oil Co.* v. *Khan*, 118 S. Ct. 275, 279 (1997). This Court has found very few business practices to have "such predictable and pernicious anticompetitive effect, and such limited potential for procompetitive benefit," that they may be condemned *per se*; such treatment is justified only when "experience with a particular kind of restraint enables the Court to predict with confidence that the rule of reason will condemn it." *Ibid.*

Despite the Court's recognition that *per se* condemnation is reserved for readily identifiable and pernicious practices, it remains settled law that there is a *per se* rule — of some sort — against "group boycotts." Yet the Court has recognized that "there is more confusion about the scope and operation of the *per se* rule against group boycotts than in reference to any other aspect of the *per se* doctrine." *Northwest Wholesale Stationers* v. *Pacific Stationery & Printing Co.*, 472 U.S. 284,

294 (1985) (quoting L. SULLIVAN, HANDBOOK OF THE LAW OF ANTITRUST § 83, at 229-230 (1977)). That confusion about the contours of the proscribed conduct makes *per se* treatment illogical and insupportable. When even courts cannot determine what a label means, to use that label after the fact to prohibit business conduct outright — magnifying the prohibition with the prospect of treble damages and potential criminal prosecution — leaves businesses in an impossible situation.

As the present case amply demonstrates, the confusion about boycott doctrine provides openings for companies to salve their wounds in the marketplace by claiming that the firms that would not buy from them in fact "boycotted" them. The Second Circuit's decision is an extreme example, inviting attempts to transform every market choice into a "boycott" of those not chosen. But such excesses are predictable in the absence of a clear definition of "group boycotts" from this Court.

Klor's and *General Motors* — two antiquated decisions in which this Court applied *per se* principles to concerted refusals to deal — are the cause of much of the confusion that this Court has decried. For that reason, "the benefits of providing guidance concerning the proper application of a legal standard" (*Brooke Group Ltd.* v. *Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 230 (1993)) weigh heavily in favor of an explanation of the continuing precedential scope of those decisions.

I. VERTICAL ARRANGEMENTS INVOLVING A SINGLE MANUFACTURER OR CUSTOMER SHOULD NOT BE CONDEMNED *PER SE* AS "GROUP BOYCOTTS"

With good reason, this Court has exercised increasing caution in defining the types of business practices that may be condemned *per se* under the antitrust laws. In the context of business relationships, "easy labels do not always supply ready

answers." *BMI* v. *CBS*, 441 U.S. 1, 8 (1979). For that reason, the Court has repeatedly removed particular categories of conduct from the scope of any *per se* rule. *State Oil Co.* v. *Khan*, 118 S. Ct. 275 (1997) (maximum resale price maintenance); *Continental TV, Inc.* v. *GTE Sylvania, Inc.*, 433 U.S. 36 (1977) (vertical territorial restrictions); *NCAA* v. *Board of Regents*, 468 U.S. 85 (1984) (price fixing by participants in joint venture); *BMI*, *supra* (same).

Consistent with that trend, the Court has held that the supposed *per se* condemnation of group boycotts does not reach all concerted refusals to deal. *Northwest Stationers*, 472 U.S. at 294. The Court has recognized that boycotts "are not a unitary phenomenon," *St. Paul Fire & Marine Ins. Co.* v. *Barry*, 438 U.S. 531, 543 (1978), and that the question of which "boycotts" were *per se* violations and which were not has engendered "more confusion" than any other "aspect of *per se* doctrine." *Northwest Stationers*, 472 U.S. at 294. Such confusion — which shows that boycotts must be, and are in fact, evaluated one-by-one — cannot be reconciled with *per se* condemnation.

Because of this confusion, the Court has specifically warned that "the category of restraints classed as group boycotts is not to be expanded indiscriminately." *FTC* v. *Indiana Federation of Dentists*, 476 U.S. 447, 458 (1986). The Court has tried to limit "the *per se* approach * * * to cases in which firms with market power boycott suppliers or customers in order to discourage them from doing business with a competitor." *Ibid.*

More recently, the Court has suggested that group boycotts should be condemned *per se* only if they "involve[ ] * * * a horizontal price-fixing arrangement." *FTC* v. *Superior Court Trial Lawyers Ass'n*, 493 U.S. 411, 436 n.19 (1990). Because any "horizontal price-fixing arrangement" is independently subject to *per se* condemnation, the Court's explanation in *Trial Lawyers* indicates that there is no coherent

justification for retaining any independent *per se* rule against group boycotts.

The Second Circuit took an entirely different tack, and concluded that a single purchaser could run afoul of the *per se* rule against group boycotts by agreeing to do business exclusively with a single supplier. See Pet. App. 10a-13a & n.6. The Second Circuit misapplied one of this Court's least celebrated decisions, *Klor's*. The court of appeals believed that *Klor's* justified labeling an entirely *vertical* purchasing relationship between a single buyer and a single seller a "group boycott" of those not included in the transactions. That strange result underscores the need for this Court to clarify not only *Klor's* but also *General Motors*, the other leading case that addressed a "boycott" within a vertical distribution arrangement.

A. Two-Firm Vertical Agreements Are Not "Group Boycotts" Of Either Firm's Competitors

If the words "group boycott" are applied literally, the first question presented is easy: there is no such thing as a "group boycott" that includes only a vertical agreement between one buyer and one seller. Many courts understand this well enough: "[A] purely vertical arrangement, by which (for example) a supplier or dealer makes an agreement exclusively to supply or serve a manufacturer, is not a group boycott." *U.S. Healthcare, Inc.* v. *Healthsource, Inc.*, 986 F.2d 589, 594 (1st Cir. 1993) (Boudin, J.). See also Pet. App. 12a. In an early boycott case, this Court recognized that ending such contracts was presumptively lawful as well: a single buyer "has the unquestioned right to stop dealing with" a seller "for reasons sufficient to himself." *Eastern States Retail Lumber Dealers' Ass'n* v. *United States*, 234 U.S. 600, 614 (1914). See also *United States* v. *Colgate & Co.*, 250 U.S. 300, 307 (1919).

The Court more recently has defined the types of boycotts that concern the antitrust laws in plainer terms. Illegal boycotts involve refusals by multiple firms with market power to deal with their "suppliers or customers in order to discourage" the suppliers or customers "from doing business with a competitor" of the *boycotting* firm. *Indiana Dentists*, 476 U.S. at 458. That was the original understanding. See *Loewe* v. *Lawlor*, 208 U.S. 274, 294 (1908) (defining boycotts as "restraints of trade aimed at compelling third parties and strangers involuntarily not to engage in the course of trade except on conditions that the combination imposes"). And that conception is consistent with this Court's observation in *Hartford Fire Ins. Co.* v. *California*, 509 U.S. 764, 800-804 (1993), that a "boycott" must involve some collateral objective, not merely an effort to seek particular terms in particular transactions.[2] By contrast, in this case Discon alleged a simple bilateral exclusive-dealing arrangement between one supplier and its customer. NYNEX's choice of another supplier over Discon was not intended to induce Discon to do anything or to have any effect on competitors of NYNEX.[3]

Before coming to this Court, Justice Breyer observed that "courts have judged the lawfulness of contracts to purchase not under per se rules but under a 'rule of reason.'" *Barry Wright Corp.* v. *ITT Grinnell Corp.*, 724 F.2d 227, 236 (1st Cir. 1983). No "vertical restraint is * * * illegal *per se* unless it includes some agreement on price or price levels" that might invoke the *per se* rule against *resale* price maintenance. *Business Electronics Corp.* v. *Sharp Electronics Corp.*, 485 U.S. 717, 735-736 (1988). Indeed, this Court has explicitly

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[2] Indeed, one of this Court's earliest decisions under the Sherman Act *refused* to condemn an agreement by members of a livestock exchange not to deal with non-members, where no collateral objective was at issue. *Anderson* v. *United States*, 171 U.S. 604 (1898).

[3] Whatever it may be called, the refusal of a buyer (or of many buyers) to purchase from a particular seller is not a *boycott* unless the refusal is designed to achieve an anticompetitive end in the market at the *buyers'* level. See *Adaptive Power Solutions, LLC* v. *Hughes Missile Systems Co.*, ___ F.3d. ___, 1998 WL 172774, at *2-*3 (9th Cir. Apr. 15, 1998).

distinguished a two-firm vertical agreement from the "group boycotts" involved in *Klor's* and *General Motors*. See *id.* at 734. Like other vertical nonprice restraints, the alleged agreement that Discon challenged — a mere agreement by a buyer to purchase only from a particular seller — should be analyzed under the rule of reason. See *Continental TV, Inc.* v. *GTE Sylvania, Inc.*, 433 U.S. 36, 57-59 (1977). Even if the purchase contract amounted to an "exclusive dealing arrangement[ ]," the rule of reason would apply. *Jefferson Parish Hosp. Dist. No. 2* v. *Hyde*, 466 U.S., 2, 29-30 & n.51 (1984); *id.* at 44-45 (O'Connor, J., concurring) (citing *Tampa Electric Co.* v. *Nashville Coal Co.*, 365 U.S. 320, 333-335 (1961)).

The Second Circuit expanded "the category of restraints classed as group boycotts * * * indiscriminately" (*Indiana Dentists*, 476 U.S. at 458) to encompass a two-firm vertical exclusive-purchasing contract. That seeming disregard for this Court's contrary instructions — and in particular the suggestion by the court of appeals that *per se* analysis could extend to such cases (see Pet. App. 11a & n.6) — invites antitrust litigation and threatens treble damages every time a buyer selects one seller over another. A disappointed dealer could characterize *every* exclusive distributorship and *every* requirements contract as a "group boycott" that the buyer and seller would be at pains to distinguish from the new category of *per se* offenses.[4] That result has no basis in current law.

B. The Rationale Of *Klor's* and *General Motors* Conflicts With Later Decisions Of This Court

Klor's and *General Motors* transplanted group boycott analysis — and *per se* condemnation — to essentially vertical arrangements that do not come within the boycott definition enunciated in *Indiana Dentists*. The reasoning of *Klor's* and

[4] The United States and the FTC agree that "a two-firm vertical restraint to exclude a supplier * * * cannot properly be termed a group boycott" because such a broad definition would encompass "[v]irtually any requirements contract." U.S./FTC Cert. Br. 14 & n.11.

General Motors is even more out of step with the Court's suggestion in *Trial Lawyers* that *per se* treatment is limited to refusals to deal which support price-fixing agreements. Although most of the reasoning in *Klor's* and *General Motors* has not survived this Court's modern antitrust jurisprudence, the two decisions have not been expressly overruled. Unsound statements in the two opinions remain available for misapplication by lower courts. Even if this case on its facts is not so close to either precedent to require reexamination of their actual holdings, the Court should expressly disapprove their flawed reasoning to forestall future misunderstandings.

1. In *Klor's*, the Court discerned (and condemned *per se*) a "group boycott" in a retailer's allegation that, at the urging of a single competing retailer located next door to the plaintiff, appliance manufacturers and their distributors had conspired to constrict the plaintiff's supply. 359 U.S. at 209. The plaintiff alleged that only one of its own competitors was involved in the conspiracy; the alleged horizontal conspiracies involved only firms that did not compete with the plaintiff. From all appearances, the manufacturers and distributors merely chose the plaintiff's competitor over the plaintiff as their only outlet on the block containing both stores; other retailers sold the same appliances within a few blocks. See *id.* at 209-210.

Nonetheless, the Court held that the alleged agreement came within a *per se* "forbidden category" of "[g]roup boycotts." 359 U.S. at 212. The Court disregarded as irrelevant the undisputed evidence that the arrangement lacked any marketwide anticompetitive effects. *Id.* at 209-210. The asserted reason that no showing of anticompetitive effects was needed, and that no showing of procompetitive effects could justify the action, was that the agreement "cripple[d] the freedom of traders and thereby restrain[ed] their ability to sell in accordance with their own judgment." *Id.* at 212 (quoting *Kiefer-Stewart Co.* v. *Joseph E. Seagram & Sons*, 340 U.S. 211, 213 (1951)). The Court went so far as to deny the manufacturers

and distributors the ability to exercise "their own judgment" to deal with one retailer rather than its neighbor. *Ibid.* Such actions "interfere[d]" with the Court's view of a wholly atomistic but supposedly "natural flow of interstate commerce" in which each actor is entitled to deal with others whether or not they want to deal with him. *Id.* at 213. That is, because the agreement harmed a single competitor, it violated the antitrust laws even if it did not harm competition generally.

2. Seven years later, the Court extended *Klor's* to reach the attempt of a manufacturer and its authorized dealers to maintain the integrity of the authorized distribution of a single brand in a competitive market. In *General Motors*, the manufacturer had created a typical distribution system with a limited number of dealers authorized to sell its vehicles to the public. The manufacturer kept limits on the configuration of its distribution system in part by including a "location clause" in the dealer agreement, which confined a dealer's privilege to sell the manufacturer's vehicles to locations approved in advance by the manufacturer. In return for this privilege (which was not territorially exclusive), the dealers were expected to contribute substantial capital investments and to provide warranty service; in addition, the manufacturer often invested capital directly in a dealership. See 384 U.S. at 144 n.19. A few authorized dealers attempted to circumvent the distribution system and encourage free-riding on the others' services by selling vehicles to unauthorized resellers for resale to the public, or by using unauthorized resellers as agents in additional unauthorized locations. The manufacturer, together with its dealer organizations, pressured the offending dealers to end this practice.

Going beyond *Klor's*, the Court held that these efforts to maintain the integrity of a single manufacturer's distribution system amounted to a *per se* violation of the antitrust laws. In the Court's view, *per se* prohibitions applied to any concerted action that "deprive[d] others of access to merchandise which the latter wish to sell to the public." 384 U.S. at 146. Without

elaboration, the Court repeatedly equated a single brand, Chevrolets, with "the market" (*id.* at 145, 146) and held that *any* "[e]xclusion of" one or more "traders from the market by means of combination or conspiracy" violated the Sherman Act (*id.* at 146). The Court's broad statements suggested that any attempt by a manufacturer to enforce restrictions on its distribution system through the cooperation of its dealers was illegal. In effect, the Court held that the desire of a manufacturer to control its "system for distributing automobiles" (*ibid.*) necessarily had to yield before the desire of a few dealers to evade that system by free-riding on the others.[5]

3. The Court in *Klor's* and *General Motors* interpreted the antitrust laws as a guarantee to particular competitors of complete freedom to structure their businesses however they liked. It since has become "axiomatic," however, "that the antitrust laws were passed for the protection of competition, not competitors." *Brooke Group Ltd.* v. *Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 224 (1993) (internal quotation marks omitted). That axiom alone should demolish the Second Circuit's suggestion that the "group boycott" label (and *per se* treatment) might apply to any contract that "seeks to disadvantage the direct competitor[s]" of one of the contracting parties. Pet. App. 11a. All contracts necessarily disadvantage "direct competitor[s]" by giving the contracted-for business to one party and not to someone else. That factor has no place in reasoned antitrust analysis, much less as part of a *per se* inquiry.[6]

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[5] The Court also viewed the conduct in *General Motors* as resale price maintenance, though it addressed pricing only as an afterthought. See 384 U.S. at 147-148; see also *id.* at 148-149 (Harlan, J., concurring in the result). It is doubtful that the conduct in *General Motors* could be characterized as resale price maintenance after *Monsanto* v. *Spray-Rite Service Corp.*, 465 U.S. 752 (1984), and *Business Electronics*.

[6] Unlike the essential concept of freedom *from legal restraints* on engaging in particular marketplace transactions, a generalized notion of "freedom" from any *contractual* restraints on future market behavior is not

The Court not only has eliminated the central rationale for *Klor's* and *General Motors* (and, thus, the decision below) but also has limited the sweeping condemnation of refusals to deal in two ways. First, the Court has removed all vertical nonprice restraints from the scope of the *per se* rule. Second, the Court has repeatedly narrowed the scope of conduct that falls within the *per se* prohibition of "group boycotts."

This Court in most respects has abandoned its brief but unjustified hostility towards the ability of manufacturers to organize and restrict the distribution of their products. The Court now substitutes an inquiry into the "demonstrable economic effect" of a practice on *interbrand* competition for its earlier "formalistic line drawing." *Continental TV, Inc.* v. *GTE Sylvania, Inc.*, 433 U.S. 36, 59 (1977). In *Sylvania*, the Court held that no *per se* rule prevented a single manufacturer from enforcing a system of location clauses almost identical to the one that was rendered unenforceable in *General Motors*. The Court had explicitly prohibited all territorial restrictions *per se* a year after deciding *General Motors*. See *United States* v. *Arnold, Schwinn & Co.*, 388 U.S. 365 (1967). The Court overruled *Schwinn* because the earlier decision had not "distinguish[ed] among the challenged restrictions on the basis of their individual potential for intrabrand harm or interbrand

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a meaningful antitrust criterion: all contracts restrict the latter "freedom." See *National Society of Professional Engineers* v. *United States*, 435 U.S. 679, 687-688 (1978). Rather than condemn particular practices based on vague notions of business "freedom," the Court has inquired whether they can be predicted with confidence to have negative consequences for consumer welfare, recognizing that "Congress designed the Sherman Act as a consumer welfare prescription." *Reiter* v. *Sonotone Corp.*, 442 U.S. 330, 343 (1979) (internal quotation marks omitted). Although the Court has proceeded cautiously and applied its new focus to particular categories of restraints one by one, the Court's focus on consumer welfare has driven it inexorably toward agreement with former Assistant Attorney General Baxter's trenchant observation that "[a] vertical problem is either a horizontal problem in disguise or no problem at all." Quoted in Meadows, *Bold Departures in Antitrust*, FORTUNE, Oct. 5, 1981, at 180, 182.

benefit." 433 U.S. at 52. In the face of the "substantial scholarly and judicial authority support[ing] the[ ] economic utility" of single-brand vertical restrictions and the "relatively little authority to the contrary," the Court found it impossible to condemn such restrictions *per se*. *Id.* at 57-58.

Significantly, the Court in *Sylvania* rejected the view, central to both *Klor's* and *General Motors*, that vertical restraints should be *per se* illegal whenever they prevent any independent business from doing exactly what it wants. Cf. *Sylvania*, 433 U.S. at 66-69 (White, J., concurring). In addition, *Sylvania* indicated that the rule of reason governs the antitrust analysis of all vertical nonprice restraints (which include a variety of exclusive arrangements) and thereby made clear that the *per se* rule does not apply to every arrangement that could be characterized as a concerted refusal to deal.

4. More recently, the Court has observed that antitrust courts cannot justify applying a *per se* rule to any concerted refusal to deal simply by invoking the "group boycott" label. "[N]ot every cooperative activity involving a restraint or exclusion will share with *per se* forbidden boycotts the likelihood of predominantly anticompetitive consequences." *Northwest Stationers*, 472 U.S. at 295. Even a plaintiff alleging that a group of its horizontal competitors agreed to exclude it from some advantage "must present a threshold case that the challenged activity falls into a category likely to have predominantly anticompetitive effects." *Id.* at 298. Rule-of-reason analysis would apply, for example, to a buying cooperative's enforcement of restrictions on its membership unless the excluding members possessed "market power or exclusive access to an element essential to effective competition." *Id.* at 296. Thus, by requiring a case-by-case demonstration of the likelihood that each alleged "group boycott" would have anticompetitive effects, and by insisting on a threshold showing of market power, the Court squarely rejected the limitless *per se* rule outlined in *Klor's* and *General Motors*. See *Rothery Storage & Van Co.* v. *Atlas Van Lines, Inc.*, 792 F.2d 210,

215-216, 229 (D.C. Cir. 1986) (Bork, J., joined by Ruth Bader Ginsburg, J.).

In *Indiana Dentists*, the Court expressly disapproved the earlier practice of "forcing" a specific practice or "policy into the 'boycott' pigeonhole and invoking the *per se* rule." 476 U.S. at 458. As noted above, the Court limited the *per se* rule to "cases in which" multiple "firms with market power boycott suppliers or customers" (*i.e.*, firms at a different level of distribution) "in order to discourage them from doing business with a competitor" (*i.e.*, a firm at the same level as the boycotters). *Id.* at 458. Neither *Klor's* nor *General Motors* met those criteria.

5. The Court has "been solicitous to assure that the market-freeing effect of [the] decision in *GTE Sylvania* is not frustrated by related legal rules," including the prohibition of group boycotts. *Business Electronics*, 485 U.S. at 726. Where vertical relationships are involved, "there is a presumption in favor of a rule-of-reason standard," rebuttable only "by demonstrable economic effect * * * rather than formalistic distinctions." *Ibid.* That is because "*interbrand* competition is the primary concern of the antitrust laws." *Ibid.* (emphasis added). The Court has concluded that "a vertical restraint is not illegal *per se* unless it includes some agreement on price or price levels." *Id.* at 735-736. In addition, the Court has explicitly held that *Klor's* and *General Motors* did *not* render *per se* illegal an agreement between a manufacturer and a dealer to terminate another, price-cutting dealer. See *id.* at 734.

The vertical agreements in *Klor's* and *General Motors* did not include specific agreements on price levels. Rather, each case involved efforts by dealers to prompt manufacturers to discipline retailers who were free riding on other dealers' services.

The horizontal aspects of the agreements alleged in the two cases likewise do not imperil competition to the point of

warranting *per se* condemnation. The alleged agreements among manufacturers and distributors in *Klor's* had no discernible effect on price or output, but simply disadvantaged a single retailer who apparently offered lower prices than his full-service next-door neighbor. As Judge Easterbrook has observed, however, the "core question in antitrust is output. Unless a contract reduces output in some market, to the detriment of consumers, there is no antitrust problem." *Chicago Professional Sports Ltd. Partnership* v. *NBA*, 95 F.3d 593, 597 (7th Cir. 1996). Yet the Court in *Klor's* found entirely irrelevant the absence of effects on output or on interbrand competition — an absence of anticompetitive effects that resulted from the presence of many outlets carrying the various appliance brands within a few blocks of the plaintiff's and defendant's stores.

As for the single-brand limited distribution system at issue in *General Motors*, Judge Posner has explained that "[i]t is unrealistic to expect the manufacturer that uses location clauses and outlet restrictions in order to limit free riding to be indifferent to the dealer that circumvents the intent of the clauses by discounting." Posner, *The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality*, 48 U. CHI. L. REV. 6, 12 (1981). And this Court has recognized that it is equally unrealistic to expect dealers who comply with the manufacturer's rules and are the victims of free riding to suffer their losses in silence. Rather, the dealers, either singly or through their trade associations, must be expected to bring free riders to the manufacturer's attention with the expectation of some response: "[C]omplaints, particularly where the manufacturer has imposed a costly set of nonprice restrictions, arise in the normal course of business and do not indicate illegal concerted action." *Monsanto* v. *Spray-Rite Service Corp.*, 465 U.S. 752, 763 (1984) (internal quotation marks omitted); see also Posner, *supra*, 48 U. CHI. L. REV. at 13. Actions by participants within a single-brand distribution network that maintain the integrity of that network *promote* rather than dis-

courage *interbrand* competition. Treating those actions as suspect "horizontal" restraints creates "needless confusion" in antitrust law and deters procompetitive conduct. *Business Electronics*, 485 U.S. at 730.

6. *Klor's* and *General Motors* are relics of a bygone era. Both decisions proceeded from the premise that manufacturers could not restrict a single retailer from selling the products he wanted in the way he wanted, and thus that they could not control the distribution of their own products even in ways that did not hurt interbrand competition. Indeed, *Klor's* relied explicitly (359 U.S. at 212) on *Kiefer-Stewart* for the proposition that even manufacturer-driven agreements that "lower prices or * * * stimulate competition" are flatly illegal if they "cripple the freedom of traders and thereby restrain their ability to sell in accordance with their own judgment." But *Kiefer-Stewart* has been overruled in two separate respects: first, in *Copperweld Corp.* v. *Independence Tube Corp.*, 467 U.S. 752 (1984), the Court rejected *Kiefer-Stewart*'s holding that an agreement between a firm and its wholly owned subsidiary could amount to an illegal conspiracy; second, in *Khan*, the Court rejected *Kiefer-Stewart*'s holding that maximum resale price maintenance amounted to a *per se* violation of the Sherman Act despite its benefits to consumers. In both instances, the Court found it necessary to repudiate flawed reasoning that stemmed from unjustified hostility toward vertical restraints.

General Motors shares many of the defects of *Klor's*, but also prefigured the overruled decision in *Schwinn*. The overruling of *Schwinn* did not automatically bring down *General Motors* with it, because the distributors in *General Motors* actively protected their common interests in the preservation of the dealer system to which they agreed. But that fact does

not change the essentially vertical nature of the restraint at issue in that case.[7] See *Monsanto*, 465 U.S. at 763.

Klor's and *General Motors* now are significant principally as sources of confusion that support ill-reasoned condemnation of exclusive dealing arrangements. The Court should clarify that those cases no longer serve as valid authority beyond their particular facts, if indeed they survive to that extent.

C. This Court Should Make Clear That Nonprice Agreements Between A Supplier And Its Distributor Or Customer Are Presumptively Legal

"[T]he primary purpose of the antitrust laws is to protect interbrand competition." *Khan*, 118 S. Ct. at 282. Vertical restraints generally limit the number and conduct of distribution outlets for particular brands of products — the very conduct broadly condemned *per se* in *Klor's* and *General Motors*. Modern economic analysis confirms that such conduct ordinarily intensifies interbrand competition. R. BORK, THE ANTITRUST PARADOX 288-291 (2d ed. 1988); Marvel, *Exclusive Dealing*, 25 J.L. & ECON. 1 (1982); Posner, *supra*, 48 U. CHI. L. REV. at 11; Telser, *Why Should Manufacturers Want Fair Trade?*, 3 J.L. & ECON. 86 (1960). That is because "[t]he manufacturer shares with the consumer the desire to have distribution done at the lowest possible cost consistent with effectiveness," BORK, *supra*, at 290; it has no incentive to restrict its dealers in a way that harms their customers. Accordingly, "vertical restraints are generally more defensible than horizontal restraints" because of "the possibility that a vertical restraint imposed by a single manufacturer or wholesaler may stimulate interbrand competition even as it reduces intrabrand competition." *Khan*, 118 S. Ct. at 281.

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[7] *General Motors* disregarded the location clause that provided the framework for the vertical organization of the distribution system, but no meaningful analysis of the consumer welfare effects of the challenged actions could disregard that vital fact.

The Court should make clear that vertical agreements between a supplier and its customer, or between a manufacturer and its distributors — whether purchase contracts, exclusive-dealing arrangements, or non-price or maximum-price restrictions on the distribution of a single manufacturer's products — should be evaluated under the rule of reason and are presumptively legal in the absence of demonstrable anti-competitive effects borne by consumers. Such clear statements are needed to prevent the use of creative characterization to "frustrate[]" the "market-freeing effect" of this Court's decisions upholding vertical nonprice restraints. *Business Electronics*, 485 U.S. at 726.

Adopting a rule of presumptive legality for vertical non-price agreements between a single manufacturer and its chosen suppliers or dealers would help ensure that legitimate procompetitive conduct is not deterred by the threat of treble-damage antitrust liability. The amorphous legal standards for the boycott rule increase that risk. See Baumol & Ordover, *Use of Antitrust to Subvert Competition*, 28 J.L. & ECON. 247, 254 (1985). In particular, "[v]ertical relations between a manufacturer and [its] dealers have been a subject of frequent litigation, often of doubtful merit." *Id.* at 263. The lack of clear guidance can lead to many years of contentious, expensive, and ultimately counterproductive litigation. See Easterbrook, *The Limits of Antitrust*, 63 TEX. L. REV. 1, 23 (1984) (noting that *Sylvania* lasted more than a decade); see also, *e.g.*, *Brunswick Corp.* v. *Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477 (1977) (damages aspect of lawsuit terminated after 11 years because of this Court's unanimous determination that the lawsuit did not allege injury of the type the antitrust laws were designed to prevent).

A vertical nonprice agreement between a single supplier and its distributor, or a purchaser and its chosen sole supplier, poses no danger to competition. To the contrary, the virtues of such restraints have long been known. See *Sylvania*, 433 U.S. at 36. Indeed, there is substantial authority for the proposition that vertical restraints in general, and particularly exclusive or restricted distribution arrangements, should be presumptively legal, if not legal *per se*. As Judge Posner explained, "in no case * * * has a purely vertical restriction on competition been shown to be anticompetitive." Posner, *supra*, 48 U. CHI. L. REV. at 22. Rigorous analysis bears out this conclusion; Judge Easterbrook reported from his independent review that, "in every vertical case in which modern econometric methods have been used, the economists found that the practices expanded output." Easterbrook, *supra*, 63 TEX. L. REV. at 32. Judge Bork put the issue in a nutshell: "[A]ll vertical restraints are beneficial to consumers and should for that reason be completely lawful." BORK, *supra*, at 297. Other commentators agree. Marvel, *supra*, 25 J.L. & ECON. at 25 ("exclusive dealing ought * * * to be treated as legal, per se"); Posner, *supra*, 48 U. CHI. L. REV. at 6; Baxter, *The Viability of Vertical Restraints Doctrine*, 75 CAL. L. REV. 933, 947 (1987) ("all vertical arrangements should be presumed benign"); Bock, *An Economist Appraises Vertical Restraints*, 30 ANTITRUST BULL. 117, 138-140 (1985) ("vertical arrangements should be viewed as competitive" in the absence of supplier monopoly or cartel).

Purely vertical restrictions are unlikely to harm consumers: a manufacturer "gains nothing by reducing competition in the distribution of its product, though it may gain from redirecting that competition from price to service." Posner, *supra*, 48 U. CHI. L. REV. at 6. Likewise, a company that chooses to buy its supplies of a particular input from one supplier rather than many will invariably do so because it perceives that doing so will serve its own best interests. Those interests are closely aligned with — not antithetical to — the consumer's interest in the production of high-quality goods or services at the lowest feasible cost.

Indeed, this Court has recognized that nonprice vertical restraints pose limited risks of anticompetitive effects. In particular, there is no evidence that vertical nonprice restraints

have a cartel-facilitating effect. *Business Electronics*, 485 U.S. at 726. "Given the absence of either theoretical or empirical grounds for condemning purely vertical restrictions as anti-competitive, to declare vertical nonprice restrictions presumptively legal * * * would serve both to lighten the burden on the courts and to lift a cloud of debilitating doubt from practices that are usually and perhaps always procompetitive." Posner, *supra*, 48 U. CHI. L. REV. at 23.

This Court should reject all attempts to place on essentially vertical, *intra*brand or single-customer arrangements labels and penalties that are appropriate only for conduct that is horizontal in an *inter*brand sense. The rule of reason, weighted by a presumption of legality, should govern all agreements that are vertical in substance as well as those that are vertical in form.

D. Conduct Undertaken Within The Supply And Distribution Arrangements Of A Single Manufacturer Should Be Analyzed Under The Full Rule Of Reason, Not A Truncated And Hostile Mode of Analysis

In its *amicus* brief at the petition stage, the United States and the FTC suggested that the single exclusive dealing relationship here, if not subject to *per se* condemnation, nonetheless might be condemned after only a cursory "quick look" at any justifications advanced for it. U.S./FTC Cert. Br. 16-17 (citing *Indiana Dentists* and *NCAA* v. *Board of Regents*, 468 U.S. 85 (1984)). Such a truncated approach would penalize procompetitive business practices and is no more defensible than the Second Circuit's expansion of the *per se* rule.

The Court should emphatically reject the government's invitation to expand the domain of "quick look" analysis, which usually equates to condemnation after a "quick look," to vertical restraints. Whatever the merits of the "quick look" approach when applied to horizontal restraints, there is no call to revive the discredited tradition of judicial hostility to ver-

tical restraints, which was founded on mistrust of business conduct that may harm individual competitors but that does not harm competition as a whole.

Application of a truncated rule-of-reason analysis to the contract at issue here necessarily would reflect a judgment that such vertical arrangements nearly always are anticompetitive, so that only the most obviously procompetitive exceptions can be tolerated. But, unlike the horizontal output restrictions addressed in this Court's cases applying a "quick look" rule-of-reason analysis, the vertical supply agreement here — and the single-brand distribution arrangements challenged in *General Motors* and other cases involving the automobile industry — do *not* predictably have pernicious effects. To the contrary, exclusive supply arrangements, like exclusive or limited distribution arrangements, normally provide procompetitive benefits through decreased input prices and increased distribution services.

Neither the government nor the Second Circuit has advanced any reason why the antitrust laws should force NYNEX to divide its scrap removal business among several contractors, much less why those laws should force it to choose Discon over Discon's competitors. In the absence of any plausible and coherent allegation that the choice of one scrap remover over another had a significant and demonstrable anticompetitive effect in a relevant market, there is no sound reason for an antitrust court to second-guess NYNEX's determination of which entity can best salvage its scrap telephone lines and equipment. See *Monsanto*, 465 U.S. at 761; *Colgate*, 250 U.S. at 307.

Discon did not allege any anticompetitive effect in a facially plausible relevant market. The removal of NYNEX's scrap may be the single-customer niche that Discon wanted to serve, but to label that niche a "market" would be frivolous. Indeed, the complaint makes clear that most other telephone companies in NYNEX's position "rel[ied] on unaffiliated contractors for removals" or used their own employees (J.A. 83).

NYNEX's purchasing practices could have had no effect on competition for removal of telephone equipment generally even if that service were somehow distinct from other salvage services.

That Discon was hurt — even if NYNEX "wanted" to hurt Discon — makes no difference. Without an injury to competition in a relevant market, Discon's misfortunes and NYNEX's alleged misconduct are of no concern under the Sherman Act. See P. AREEDA & H. HOVENKAMP, ANTITRUST LAW ¶ 1644c, at 726-728 (Supp. 1997) (discussing decision below). See also *Brooke Group*, 509 U.S. at 225. They certainly do not justify a regime of judicial hostility toward single-buyer exclusive supply contracts under either a *per se* or a "quick look" approach.

II. UNCERTAINTY ABOUT "GROUP BOYCOTTS" IMPEDES PROCOMPETITIVE CONDUCT IN THE AUTOMOBILE INDUSTRY

Automobile manufacturers, like many other businesses, do not deal with everyone who offers materials or who wishes to sell newly manufactured vehicles. To the contrary, automobile manufacturers have realized far greater efficiencies by purchasing in greater volumes from a limited number of authorized parts suppliers, and in selling new vehicles through a coordinated network of a limited number of authorized dealers. "Most economists recognize that * * * much private litigation surrounding the[ ] use [of vertical restraints] involves contract disputes rather than antitrust problems." Klein & Murphy, *Vertical Restraints As Contract Enforcement Mechanisms*, 31 J.L. & ECON. 265, 295 (1988). If this Court does not clarify the confusion about group boycotts that led to the decision below, such misuses of the antitrust laws to hamper efficiency will only increase in frequency.

A. The Continuing Confusion Surrounding "Group Boycotts" Impedes The Ability Of Automobile Manufacturers To Preserve The Quality And Integrity Of Their Dealership Networks

New automobiles are sold in the United States almost exclusively through networks of independent, franchised local dealers. All manufacturers limit the number of dealers who have the right to sell each manufacturer's new vehicles; most dealers compete with other authorized dealers for the same make within a given geographic area.

Manufacturers require their dealers to invest substantial capital to acquire and maintain their authorized dealerships. Because of the expensive services manufacturers typically require their dealers to provide, the automotive industry is often cited as a classic example of an industry in which free riding can pose a substantial problem. *E.g.*, *Sylvania*, 433 U.S. at 55; Kelly, *The Role of the Free Rider in Resale Price Maintenance, the Loch Ness Monster of Antitrust Captured*, 10 GEO. MASON U. L. REV. 327, 361 (1988).

Dealers must expend substantial sums to purchase, staff, and equip their showrooms. The facility must be sufficiently spacious and well lit to display the vehicles in an attractive fashion. Modern showrooms also contain audiovisual displays to provide consumers with in-depth information about specific models. Manufacturers require dealers to maintain an adequate vehicle inventory, with an appropriately broad range of models and colors. And dealers are responsible for hiring and keeping a sufficient number of knowledgeable salespeople, who often are required to attend manufacturer-designed courses to learn about the various models. The sales staff may need follow-up and refresher training each new model year.

In addition, dealers generally must make substantial investments in advertising and promotional activities, including community sponsorships, that are designed to generate good will and to inform the public regarding the availability

and attributes of the manufacturer's automobiles. Among the extensive post-sale services that dealers provide are a service department and parts inventory to handle warranty repairs and maintenance, and to keep replacement parts available to vehicle purchasers and independent mechanics. Manufacturers often require that parts and service departments meet specific standards in tools and equipment, and maintain a staff with appropriate technical certification and training.

Manufacturers cannot effectively compete in the nationwide, interbrand automobile market without a widespread network of dealers offering high-quality services. By characterizing as a "group boycott" a simple choice of one vertical business relationship over another, the decision below would place a powerful constraint on a manufacturer's ability to ensure that its dealers provide the services that customers typically demand. Maintaining that level of services may require the manufacturer to limit the number of outlets in a particular area, despite the eagerness of a prospective dealer to carry the manufacturer's brand. Manufacturers need to be able to use "vertical restraints ancillary to exclusive [or partly exclusive] dealing," such as "[c]ooperative advertising, warranty registration, and repair restrictions[,] * * * in order to charge dealers more efficiently for manufacturer promotional efforts." Marvel, *supra*, 25 J.L. & ECON. at 10.

To attract and retain well-financed and service-intensive dealers, a manufacturer may have to prevent some dealers from free riding on their peers' services. Free-riding dealers may offer the lower vehicle prices that substandard service costs would permit, or may increase their own volume by selling at wholesale to brokers or other non-dealers who free ride on the services of other dealers. Under the rules advanced by the Second Circuit and the government, however, a manufacturer that took any action against free-riders to preserve the integrity of the dealer network would expose itself to an antitrust lawsuit on the theory that it and one or more authorized dealers engaged in a group boycott against the prospective dealer or the free rider.

Litigation of a type that flourished before *Sylvania* and *Sharp* — and still is not unusual — could flourish anew using the "group boycott" label to attack the manufacturer's freedom to market its products as it sees fit, with or without prompting from its current dealers. Disgruntled dealers and dealer-applicants have not hesitated to enlist the antitrust laws in attempts to override manufacturers' choices — all of which might be forced into the "boycott" category if the Second Circuit's decision were affirmed. See, *e.g.*, *Lovett* v. *General Motors Corp.*, 998 F.2d 575 (8th Cir. 1993), cert. denied, 510 U.S. 1113 (1994); *Arnold Pontiac-GMC, Inc.* v. *General Motors Corp.*, 786 F.2d 564 (3d Cir. 1986); *Parsons* v. *Ford Motor Co.*, 669 F.2d 308 (5th Cir.), cert. denied, 459 U.S. 832 (1982); *Quality Mercury, Inc.* v. *Ford Motor Co.*, 542 F.2d 466 (8th Cir. 1976), cert. denied, 433 U.S. 914 (1977); *Tunis Bros. Co.* v. *Ford Motor Co.*, 696 F. Supp. 1056 (E.D. Pa. 1988) (denying Ford's motion for summary judgment on group boycott claim because of confused legal standard under both *per se* rule and rule of reason), later decision, 952 F.2d 715 (3d Cir. 1991), cert. denied, 505 U.S. 1221 (1992).

In substance, these lawsuits are either breach-of-contract claims or simple efforts to force a manufacturer to alter its distribution system for the benefit of the plaintiff. To forestall these misuses of the antitrust laws, this Court should make clear that, so long as interbrand competition is robust, all vertical nonprice agreements between a manufacturer and its dealers are presumptively legal.

B. The Confusion Surrounding "Group Boycotts" Impedes The Ability Of Automobile Manufacturers To Contract Efficiently With Suppliers

Automobile manufacturers depend on close, mutually advantageous relationships with their parts suppliers. The automotive industry uses hundreds of thousands of parts made by

tens of thousands of approved suppliers. Many of these parts are made to precise specifications, with tolerances as close as a few thousandths of an inch. Manufacturers thus cannot, by and large, buy component parts off the shelf, but rather must have parts made to the specifications for a particular vehicle. To provide incentives for high standards of compliance, and to allow suppliers to take advantage of efficiencies of scale that result in lower part prices, automobile manufacturers routinely enter into exclusive or partially exclusive sole- or second-source arrangements for the supply of particular parts. It is a matter of great concern to the industry if a manufacturer that terminates one supplier in favor of another may face treble-damages "group boycott" litigation in addition to a contract dispute.

Automobile manufacturers also impose demanding delivery requirements. Many major manufacturers now use a "just-in-time" system, in which parts must arrive at the factory just before vehicles are assembled. "Just-in-time" systems produce substantial savings through reduced parts inventories and fewer assembly line delays. But to run this type of supply system requires close computer coordination between the manufacturer and its suppliers. In many cases, the computers of suppliers and manufacturers are linked so that design and shipping data can be electronically communicated.

Because the design and supply of parts now depends so substantially on the interaction of computer systems, automobile manufacturers have taken action to prevent any disruptions in automobile production by the "Year 2000 problem," which may immobilize some computers in less than two years. Many of the manufacturers' efforts come within the framework of the Automotive Industry Action Group ("AIAG"), a non-profit trade association of vehicle manufacturers and their suppliers that encourages technological improvements to increase efficiency in production. Among other projects, the AIAG has provided self-assessment surveys to more than 65,000 suppliers to ascertain whether they have

developed workable plans to respond to the Year 2000 problem. Some manufacturers are conducting follow-up audits to obtain a first-hand look at the scope of the problem, which is complicated further by the fact that many first-tier suppliers purchase their own materials and parts from second-tier firms on whose computer systems the first-tier suppliers depend.

The AIAG collects and appraises suppliers' survey responses, evaluating them in light of certain quantitative standards for remedial activity. The AIAG then classifies suppliers by the degree of risk the Year 2000 problem presents to their ability to maintain continuity of supply, identifying as "high risk" those suppliers that are least prepared to respond to the Year 2000 problem. Although the AIAG is collectively gathering data from the *suppliers*, each manufacturer *separately* determines whether its suppliers are taking sufficient steps to ensure that their computer systems will be sufficiently reliable to ensure continuing compliance with the tight manufacturing tolerances and just-in-time delivery schedules demanded by modern automotive manufacturing.

In the near future, a manufacturer quite possibly may determine, based in part on data collected by AIAG, that a supplier's response to the Year 2000 problem was inadequate and thus presents an unacceptable risk to the manufacturer's business. As a result, the manufacturer may change suppliers. If this Court does not further clarify "group boycott" in deciding the present case, it is easy to anticipate a flurry of lawsuits by disappointed suppliers who allege that their replacement constitutes a group boycott by their manufacturer and the new supplier, if not a group boycott by all of the manufacturers and suppliers in AIAG.

But the antitrust laws, and group boycott law in particular, should not affect a manufacturer's ability to decide to buy parts only from suppliers with computer systems adequate to support the manufacturer's production process. The decision below may well make such a choice into the basis of a long-running and expensive, if ultimately unsuccessful, antitrust

action, unless this Court reverses that decision in a way that forecloses future misapplications of *Klor's* or *General Motors*.

III. FACIALLY DEFECTIVE ANTITRUST ACTIONS ARE APPROPRIATELY DISMISSED UNDER RULE 12(b)(6)

Antitrust plaintiffs bear not only a burden of proof, but a burden of coherence in alleging conduct that constitutes a violation of the antitrust laws. "[A] district court must retain the power to insist upon some specificity in pleading before allowing a potentially massive factual controversy to proceed." *Associated General Contractors* v. *California State Council of Carpenters*, 459 U.S. 519, 528 n.17 (1983). Plaintiffs are not entitled to try to extort a settlement through burdensome discovery when the strictures of Rule 11 prevent them from alleging facts that might support an antitrust claim.

The district court appropriately disposed of the complaint in this case, which attempted to transform respondent's dissatisfaction with petitioners' choice of a different service supplier into an antitrust claim by "endeavor[ing] to relitigate much of the conduct underlying the break up of old AT&T." J.A. 51. The Second Circuit recognized that "Discon cannot succeed" on the Section 1 theories it advanced. Pet. App. 10a. But rather than taking the complaint on its own terms and affirming the dismissal, the Second Circuit labored to fashion a new theory from old precedent to keep this litigation in the courts.

This Court should explicitly endorse the district court's efficient disposition of this meritless claim. In an earlier antitrust case the Court encouraged "[d]istrict courts [to] be especially alert to identify frivolous claims brought to extort nuisance settlements." *Reiter* v. *Sonotone*, 442 U.S. 330, 342 (1979). It is wholly appropriate for district courts evaluating antitrust lawsuits to "exercise sound discretion and use the tools available" to prevent harassment of business and misuse of the courts (*ibid.*) by requiring that the pleaded facts — not merely the general allegations of subjective intent that the

Second Circuit found largely sufficient (Pet. App. 11a) — add up to a coherent and sustainable theory of an antitrust violation, particularly when competitors rather than consumers are the plaintiffs. See *Dial A Car, Inc.* v. *Transportation, Inc.*, 82 F.3d 484, 487-488 (D.C. Cir. 1996) (Edwards, C.J.); *Interface Group, Inc.* v. *Massachusetts Port Authority*, 816 F.2d 9, 12 (1st Cir. 1987) (Breyer, J.) (affirming dismissal because "facts alleged" could not "make out the * * * injury to the competitive process necessary to show" an antitrust violation). "It is * * * important to find ways to *reduce* the attractiveness of antitrust as a method of raising rivals' costs." Easterbrook, *supra*, 63 TEX. L. REV. at 34 (emphasis added). The Second Circuit instead increased the attractiveness of antitrust litigation as a substitute for competition in the marketplace. This Court should take the opportunity presented here to endorse intelligent judicial scrutiny of antitrust complaints, with prompt dismissal of those that cannot survive on the facts pleaded.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

PHILLIP D. BRADY
MARK SLYWYNSKY
American Automobile Manufacturers Association
1401 H Street, N.W.
Suite 900
Washington, D.C. 20005

STEPHEN M. SHAPIRO
ROY T. ENGLERT, JR.
Counsel of Record
DONALD M. FALK
MICHAEL E. LACKEY, JR.
Mayer, Brown & Platt
2000 Pennsylvania Ave., N.W.
Washington, D.C. 20006
(202) 463-2000

Counsel for Amicus Curiae

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